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Supreme Court of the United States

October Term, 1970

No. 1098

Garfield & Co.,

Petitioner,

—against—

Francis J. Wirst,

Respondent.

BRIEF OF NEW YORK STOCK EXCHANGE AS *AMICUS CURIAE* IN OPPOSITION TO PETITION FOR WRIT OF CERTIORARI

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OCTOBER TERM, 1970

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BRIEF OF NEW YORK STOCK EXCHANGE AS *AMICUS CURIAE* IN OPPOSITION TO PETITION FOR WRIT OF CERTIORARI

This brief is submitted on behalf of New York Stock Exchange as *amicus curiae* (hereinafter "the Exchange") pursuant to Rule 42 of the Court. It is submitted with the consent of the parties.

The Interest of the Exchange

Although petitioner's contentions are in the form of objections to the arbitrators who rendered the disputed award, in reality they constitute a challenge to any Exchange arbitration and an attack on two vital provisions of the Exchange's Constitution. The first is Article VIII, Section 4, pursuant to which the Board of Arbitration was appointed. It provides:

"Sec. 4. Promptly after the annual election of the Exchange, the Chairman of the Board of Governors

shall appoint, subject to the approval of the Board of Governors, a Board of Arbitration to be composed of fifteen arbitrators selected from members and allied members of the Exchange who are not members of the Board of Governors, to serve at the pleasure of the Board of Governors or until the next annual election of the Exchange and their successors are appointed and take office."

The second provision is Article VIII, Section 5, which provides:

"Sec. 5. Any controversy between parties who are members, allied members, member firms or member corporations shall be submitted for arbitration to five Arbitrators, members of the Board of Arbitration provided for by Section 4 of this Article, and the decision of a majority of such Arbitrators shall be final. All such proceedings shall be held in the City of New York."

It is clear that if petitioner's contentions are valid as a matter of law, the Exchange arbitration system will have been seriously impaired because it is very unlikely that in petitioner's view, any arbitrator or group of arbitrators selected from the Board would be competent to sit in the present case, or, indeed, in any case arising from a dispute involving member organizations of different sizes.

Present federal policy recognizes that Exchange arbitration is an essential component of the regulation of the securities industry under the Securities Exchange Act of 1934. The SEC's 1963 Report of Special Study of Securities Markets (Pt. IV, Ch. 12), for example, pointed out that the process of Exchange arbitration is not only a vital part of the mechanism by which the Exchange regu-

lates the activities of its membership but is also cloaked with additional public importance since disputes between members and non-members, as well as those between members, may be arbitrated. The Special Study found (id. at 561) that during the two years intensively studied:

> "[T]he arbitration director acting for the Exchange performed his ministerial functions without favoring either side and . . . there was no lack of impartiality on the part of the arbitrators."

It is because petitioner's challenge to this group of arbitrators constitutes a challenge to its Constitution and to the procedures established thereunder that the Exchange has submitted this Brief as *amicus curiae*.

ARGUMENT

POINT I

The alleged business relations of which petitioner complains were not such as to warrant disclosure.

The gravamen of petitioner's argument apparently lies in the arbitrators' alleged failure to advise petitioner of the business relationships between them and Spear, Leeds & Kellogg (hereinafter "Spear"). Initially, it should be noted that the kind of business relationships of which petitioner complains would have involved the purchase or sale of securities by one or more of the arbitrators or his or their firms, directly or indirectly, from Spear as specialist. The relationship would arise not through exercise of a choice on the part of the non-specialist member but rather in the usual and unavoidable course of business, *i.e.*, because Spear, in the exercise of its function as a specialist, is responsible for maintaining an inventory of

and market for stocks in which it specializes. Such dealing is not the kind of business relation which—even assuming petitioner's ignorance of specific transactions—gives rise to the appearance of partiality condemned by such cases as *Commonwealth Coatings Corp.* v. *Continental Casualty Co.*, 393 U.S. 145 (1968).

In the *Commonwealth* case, the Court held that arbitrators must "disclose to the parties any dealings that might create an impression of possible bias." 393 U.S. at 149. Fundamental to the decision was the fact that the critical business relationship was voluntarily undertaken and unknown to one of the litigants.

In the present case the alleged business relations could not reasonably create an impression of possible bias for they would have been inevitable within the framework of the Exchange and obvious to all.

Furthermore, even assuming that the type of possible business relations at issue was embraced by the *Commonwealth* case, petitioner's contention that the arbitrators breached their duty by failing to disclose such relationships must fail as a matter of law because of petitioner's concession (Petition, pp. 4-5) that it knew that such relations existed. Indeed, all Exchange members know two facts when they join the Exchange and unqualifiedly agree to submit all disputes with other members to Exchange arbitration: (1) that business dealings with other members, particularly specialist members, are inevitable in the ordinary conduct of their business and (2) that the volume of such dealings will vary depending upon the size of a particular member. Thus, as petitioner concedes, the business dealings which petitioner seeks to have disclosed must have been, and were, known to petitioner for a substantial period, and there was nothing for the arbitrators to disclose.

Given the circumstances of the well-known and involuntary dealings within the Exchange's system of fixed commissions, it is submitted that it would be unreasonable to hold that because of such dealings, the arbitrators here involved, or the Exchange's Board of Arbitration generally, constituted a group which "might reasonably be thought biased against one litigant and favorable to another." 393 U.S. at 150.

POINT II

The rules established by the Court in commercial arbitration decisions were not intended to be applied in other types of arbitration proceedings, particularly when such proceedings are an essential component of a federally encouraged scheme for industrial self-government.

To apply the doctrine urged by petitioner would unreasonably burden a vital component of the securities industry's supervisory and regulatory system and, therefore, would contravene the public policy of the United States.

The Court has held that arbitration doctrines which are salutary in the field of commercial arbitration should not be uniformly applied to other fields where arbitration is a component of an industry's attempt at self-regulation. In *United Steelworkers of America* v. *Warrior & Gulf Navigation Co.*, 363 U.S. 574 (1960) the union had brought a suit to compel arbitration of an alleged grievance. The Supreme Court stated that the federal courts should not hesitate to enforce the use of the arbitration provision in a collective bargaining agreement because federal policy favored industry arbitration in the labor area as distinguished from the general commercial area and added ". . . thus the run

of arbitration cases . . . becomes irrelevant to our problems." 363 U.S. at 578. The Court emphasized that the arbitration of labor disputes " . . . has quite different functions from arbitration under an ordinary commercial agreement" because it plays a vital role in a federally encouraged effort to erect a system of industrial self-government. The Court concluded its analysis with the following quotation from Dean Shulman's study of the arbitration process in the labor field:

> " 'A proper conception of the arbitrator's function is basic. He is not a public tribunal imposed upon the parties by superior authority which the parties are obliged to accept. He has no general charter to administer justice for a community which transcends the parties. He is rather part of a system of self-government created by and confined to the parties . . . .' " 363 U.S. at 581.

It is clear that under the Securities Exchange Act of 1934 the role of the arbitrator in the securities field is substantially similar in this respect to that of the arbitrator in the labor field. Section 28(b) of the Securities Exchange Act of 1934 provides that nothing in the statute "shall be construed to modify existing law (1) with regard to the binding effect on any member of any exchange of any action taken by the authorities of such exchange to settle disputes between members. . . ." It has been noted by Professor Loss that this provision reflects a Congressional policy favoring arbitration which is apparently based more upon an appreciation of the unique and sensitive nature of dealings between Exchange members than upon arbitration's ordinary advantages of speed and economy. Loss, *Securities Regulation*, p. 1814 fn. 430 (2d ed. 1961). The nature of the securities industry and, indeed, that of the Exchange community, is complex. The arbitration proceedings which are

directed at supervising the actions of a member, allied member, or member organization will often entail questions concerning customs, usages, and procedures, as well as Exchange rules, which are unique to the industry or to the Exchange itself. It is, therefore, particularly appropriate that the arbitration panel which is to hear and determine a case involving a dispute between Exchange members or member organizations be comprised of members or allied members of the Exchange since such persons occupy positions similar to those of the disputants and are knowledgeable concerning the often unique features of the industry in general, and of the Exchange community in particular.

Petitioner's arguments could well sweep away this body of expert decision-makers and thrust upon the courts or laymen the task of deciding often complex and technically difficult issues.

CONCLUSION

As the decision of the Court of Appeals is fully supported by the relevant authorities, public policy and common sense, the petition should be dismissed.

Respectfully submitted,

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REPLY

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PETITIONER'S REPLY BRIEF

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Supreme Court of the United States

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PETITIONER'S REPLY BRIEF

Respondent's brief in opposition is beside the point. By reason of the business dealings petitioner endeavored to avoid the arbitrators on the only basis available under the Constitution of the Exchange and court decisions then extant; the Court of Appeals held that petitioner "properly and timely raised its objections under the circumstances and the then existing state of the law." (18a).

The real question before the Court is whether it wishes to leave in effect as an authoritative exposition of the Arbitration Act and its own decision in *Commonwealth Coatings Corp.* v. *Continental Casualty Co.*, 393 U.S. 145 (1968), in that Judicial Circuit in which not only the Exchange is located but which is also the greatest center of trade associations and commercial and maritime arbitration, the following passage in the opinion of the Court of Appeals (18a):

> "We disagree [with petitioner] for we find that such objections [objections to business dealings] were waived in advance by Garfield and by all other members of the Exchange.
>
> "Garfield, when becoming a member firm of the Exchange, agreed to the arbitration of disputes according to the Exchange Constitution and Rules."

Neither respondent nor the Exchange come to grips, in its application to the facts of this case, with the doctrine of *People ex rel. City of New York* v. *Nixon*, 229 N.Y. 357, 361-362, that, "The obligation of a contract is determined by the law in force when it is made . . . Statutes then existing . . . do not change the obligation. They make it what it is." (petition, pages 11-12).

The Exchange argues, in substance, that the application of *Commonwealth Coatings* would wreck a useful system. The experience of the Society of Maritime Arbitrators has been that *Commonwealth Coatings* is invoked only infrequently. The American Arbitration Association had already adopted the doctrine of *Commonwealth Coatings*. If the Exchange system is as useful as claimed we can be confident that, as with the Society of Maritime Arbitrators, *Commonwealth Coatings* will not often be availed of; if it is constantly availed of, we can be sure that the system is not as valuable as the Exchange claims and has been imposed upon a reluctant membership by a powerful hierarchy.

In any event, there are plenty of people in New York who are familiar with the techniques of the Exchange, moreover, from time to time there are disputes such as the present which involve issues of law for which the courts are more suited than boards of arbitration.

CONCLUSION

The Judgment Should Be Reversed.

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January 11, 1971